



The Actuarial Profession

making financial sense of the future

Consultation Response **BIS and FRC**

Proposals to reform the Financial Reporting Council

10 January 2012

About the Institute and Faculty of Actuaries

The Institute and Faculty of Actuaries is the chartered professional body for actuaries in the United Kingdom. A rigorous examination system is supported by a programme of continuous professional development and a professional code of conduct supports high standards, reflecting the significant role of the Profession in society.

Actuaries' training is founded on mathematical and statistical techniques used in insurance, pension fund management and investment and then builds the management skills associated with the application of these techniques. The training includes the derivation and application of 'mortality tables' used to assess probabilities of death or survival. It also includes the financial mathematics of interest and risk associated with different investment vehicles – from simple deposits through to complex stock market derivatives.

Actuaries provide commercial, financial and prudential advice on the management of a business' assets and liabilities, especially where long term management and planning are critical to the success of any business venture. A majority of actuaries work for insurance companies or pension funds – either as their direct employees or in firms which undertake work on a consultancy basis – but they also advise individuals and offer comment on social and public interest issues. Members of the profession have a statutory role in the supervision of pension funds and life insurance companies as well as a statutory role to provide actuarial opinions for managing agents at Lloyd's.

**PROPOSALS TO REFORM THE FINANCIAL REPORTING COUNCIL
A JOINT BIS AND FRC CONSULTATION**

RESPONSE ON BEHALF OF THE INSTITUTE AND FACULTY OF ACTUARIES

1. Introduction

1.1 On behalf of the Institute and Faculty of Actuaries (the Profession), we are grateful for the opportunity to respond to this joint consultation by the Department for Business, Innovation & Skills (BIS) and Financial Reporting Council (the FRC). In doing so, our overriding interest and concern are that any reform should serve to enhance the important relationship between the Profession and the FRC and our collective ability to serve effectively the public interest.

1.2 We welcome the proposed reforms to the FRC in so far as they advance that shared objective. However, within that context, we have a fundamental concern that the FRC's mission should be defined in contemporary terms such as to match its responsibilities, including in relation to the Profession. We are concerned that, in restricting its focus, as suggested in the Consultation Document, to "*the interests of investors in the corporate sector*"¹, the FRC's remit will be inappropriately narrow, having regard to our mutual public interest responsibility in relation to actuaries and the range of work which they undertake.

1.3 We set out in section 2 a more detailed overall response to the consultation paper. Our specific responses to the questions listed in part 6 of the consultation paper are set out in section 3 below. We highlight a number of key overarching points in our concluding remarks at section 4.

2. Overall response

We welcome:

2.1 The intention to reorganise the FRC, simplifying its structure in order better to focus its activities, thereby clarifying their scope and improving the FRC's efficiency and effectiveness. We note and welcome Jim Sutcliffe's comment

¹ Executive Summary, page 4

in his article in *the Actuary*, dated 24 November 2011, to the effect that the proposals will, “*make it easier for [us] to demonstrate that [our] regulation of actuaries and actuarial work is relevant, proportionate and consistent with the way other professions are regulated*”

- 2.2 The emphasis on rationalising and minimising the regulatory burden of which the FRC is a part, and on developing a more proportionate range of sanctions and procedures.
- 2.3 The intention to support the leadership of the professional bodies the FRC oversees (page 8, para 1.2).
- 2.4 The clarification in Jim Sutcliffe’s letter to Jane Curtis of 18 October 2011 about the intended application of the arrangements to the Actuarial Profession (although we will welcome further clarification as the proposals in the consultation document are refined – see below).

We think there could be more emphasis on:

- 2.5 Redefining the FRC’s mission in contemporary terms which match its current responsibilities, including those in respect of the Actuarial Profession. As foreshadowed in our introductory remarks, we do not think that the FRC’s mission and focus should be purely redrafted in terms of the interest of investors, whether in actuarial or in other work, important though that interest is. Equally, we consider that the mission statement places inappropriate emphasis on large/ public companies, as opposed to the other types of organisations and entities in which actuaries, accountants and auditors are engaged. Instead we suggest a broader focus on the FRC’s responsibility for promoting, in the public interest, good governance in companies and good regulation in the accountancy and actuarial professions.

We note, and are encouraged by, the recognition at paragraph 2.3 of the consultation paper of the important role which actuaries are increasingly playing in relation to risk management. We also welcome the statement by Jim Sutcliffe, in his article in *the Actuary*, dated 24 November 2011, to the effect

that;

“the proposals are not about changing the scope of [our] activities in relation to actuaries and actuarial work, and [we] will continue to maintain a strong actuarial team to ensure that the TASs are fit for purpose, to provide input to international initiatives, and to monitor the way the Profession regulates its members”.

We should therefore welcome a mission statement which is more appropriately balanced and reflective of this approach and of the broad range of activities in which actuaries (as well as accountants and auditors) are engaged.

- 2.6 The commitment to exercise the FRC's regulatory responsibilities in accordance with the Good Regulation Principles. We welcome the reference to this in paragraph 1.2 of the document but suggest it could be strengthened.
- 2.7 Subsidiarity, and not just in terms of leaving all but the most significant public interest cases to the disciplinary processes of the relevant professional body.
- 2.8 The implications for the FRC's role of the increasing globalisation of regulation.

We have specific concerns about:

- 2.9 The limited recognition in the Consultation Document of the FRC's role in relation to actuarial work and the lack of initial clarity about which aspects of the document were intended to apply to the Actuarial Profession. Nevertheless, we are grateful for the supporting letter of explanation and article in *the Actuary* from Jim Sutcliffe.
- 2.10 The suggestion (at page 6 of the Executive Summary) that "*the FRC should be able to take disciplinary action against individuals or firms without the need for a full tribunal hearing provided that this would not be contrary to the public interest and the parties agree*". Recognising, as this statement does, that parties' consent is not the only consideration in determining whether to hold a full/ public hearing, we would be grateful for clarification as to how and by whom the public interest in this context is to be assessed. In the context of tribunal proceedings, we suggest that this should include consideration of the interests of justice; in particular where there is any inequality insofar as one of the parties is not legally represented. Whilst supporting proportionality in relation to enforcement, we have a wider concern that this should not be to the detriment of regulatory transparency, in the public interest.
- 2.11 Whilst we welcome the assurance in the letter from Jim Sutcliffe, as well as in his article in *the Actuary* and in paragraph 2.4 of the consultative document, that the FRC is not seeking to change the scope of its activities in relation to the Actuarial Profession (including its standard setting, oversight or disciplinary role), we note that the letter qualifies the statement by saying that it is accurate "at this stage".

- 2.12 The scope and nature of the proposed supervisory enquiries and the possible new powers mentioned in section 5.12 of the consultation document. We are unclear how the FRC proposes to decide when and by what means to undertake “*supervisory inquiries at its own initiative into significant matters of concern*” (page 6 of the Executive Summary) and to what extent this proposal might relate to actuaries. In particular, it would be helpful to understand how assurance will be provided to stakeholders (including the public) that any such inquiries are proportionate in scope and appropriately targeted (at areas of identified risk), and that there will be an appropriate level of consultation before they are put in hand.

We should welcome greater clarity about:

- 2.13 The important distinction- both conceptually and in terms of its impact on policy and approach- between the FRC’s respective regulatory and oversight roles. It would be helpful to have greater clarity as to how this distinction is reflected in the FRC’s strategy. (Reference is made for example to paragraph 1.3, where it is said that, “*Independence from the professions and others, whose activities it regulates, is crucial for public confidence in its regulatory effectiveness*”.)
- 2.14 The criteria and procedure relating to the approval of TAS’s (see paragraph 3.9 of the consultation document). We assume, but should welcome clarification, that the planned post-implementation review of existing TAS’s will be unaffected by the proposed changes.
- 2.15 Any envisaged implications for the Actuarial Profession of the proposed changes to disciplinary arrangements in relation to the accountancy profession.
- 2.16 The precise balance of membership of the Expert Advisory Councils and the representation of actuarial knowledge and skills in the membership of the FRC Board and its two key committees, including the position of Observers.
- 2.17 The relative roles envisaged for the Executive and for Advisory Councils in the new structure.
- 2.18 Any proposals for developing and strengthening the FRC’s Actuarial User Committee.
- 2.19 The future funding arrangements for the FRC (paragraphs 3.19 - 3.20 of the document).

3. Specific Responses to Consultation Questions

Our specific responses to the questions listed at part 6 of the Consultation Document are as follows, but are to be read in conjunction with the comments and concerns we have expressed in sections 1 and 2 above. We additionally respond separately and on the same basis below to the specific questions posed by Jim Sutcliffe in his article in *the Actuary*, dated 24 November 2011.

The case for FRC reform

[1] Do you have any comments on the case for FRC reform as set out in this document?

We support the case for reform described in the document. In particular, we welcome the statement of the FRC's regulatory approach in paragraph 1.2, especially its emphasis on meeting the principles of good regulation and supporting the leadership of the professional bodies the FRC oversees in its work to raise standards.

[2] Do you agree that the proposals for reform will bring benefits and increase the effectiveness of the FRC?

We hope and believe that they will do so, in so far as they should facilitate a more focused and coordinated approach, especially in relation to cross-cutting issues. It will also be essential that they are implemented sensitively and in continued dialogue with the professions which the FRC regulates and oversees.

[3] Do you have any comments on the consultation stage impact assessment?

No

An investment focus for the FRC's activities

[4] Should the primary focus for regular FRC activity in relation to codes and standards for corporate governance, accounting and auditing, and for monitoring the quality of corporate reporting and auditing, be publicly traded companies and large private companies?

The FRC's responsibilities in relation to the Profession do not focus solely on large companies but affect the work of all members of the Profession. Equally, a purely investment-related focus seems unduly narrow and therefore inappropriate in respect of these activities of the FRC (see also point 2.5 above).

[5] Is the definition of large private company for this purpose – an annual turnover of £500m or more – appropriate?

We have no specific comment, beyond the concerns which we have expressed as to the appropriateness of the proposed focus on large companies.

[6] Should the scope of the FRC's accountancy disciplinary arrangements be narrowed to cover the quality of work and conduct of accountants in relation to the preparation and audit of annual reports and other reports for the capital markets, leaving other cases of potential misconduct to the professional bodies?

We have no comment.

[7] Are there other areas of activity from which the FRC could appropriately withdraw?

We have no specific proposals to make at this time. The FRC's responsibilities in respect of the Actuarial Profession are still relatively new and we wish to see them evolve organically and by mutual agreement, as circumstances, needs and relationships develop.

A streamlined structure

[8] Do you agree that streamlining the FRC's governance and structure will bring the benefits described?

We hope that it will do so.

[9] Do you have any comments on the proposed reformed FRC governance and structure?

Please see our earlier comments. In particular, whilst we welcome the streamlining, we seek reassurance (including confirmation of that already offered verbally) in respect of the adequate and consistent representation of qualified actuarial opinion in the “Expert Advisory Councils” - which are to underpin the work of the Codes and Standards Committee and, to a lesser degree, the Conduct Committee - and in those Committees themselves. We also seek reassurance that appropriate safeguards will be built in to the new procedural arrangements, to ensure that the views of the advisory councils will not be lightly disregarded either by the FRC’s executive committees or by members of its executive staff.

Independent supervisory and disciplinary arrangements

[10] Do you agree the FRC should be given powers to determine and require a recognised supervisory body to impose proportionate sanctions, subject to appropriate safeguards, on an audit firm and/or individual auditor in respect of poor quality work?

We understand that the proposals reflected in questions 10-13 relate purely to the accountancy profession. In so far as the FRC might in future consider relating any such arrangements to the members of the Actuarial Profession, we believe that it would be essential to consult with and gain the agreement of the Profession before proceeding.

[11] If not, what are your concerns and how do you believe this issue should be addressed?

Not applicable.

[12] Do you agree the FRC should have the ability to make its own rules for the independent disciplinary arrangements without being required to obtain the agreement of the professional bodies?

Not applicable.

[13] If not, how would you propose the FRC demonstrates its independence in this regard?

Not applicable.

Proportionate regulation

[14] Should the FRC be able to take more proportionate, nuanced action against a Recognised Supervisory or Qualifying Body and therefore be given a wider range of enforcement powers against the recognised bodies? In particular, should the FRC be able to:

- *Issue an enforcement order, requiring the body to take specified actions by a specified date, without the need for a court order?*
- *Impose conditions on continued recognition as an RSB or RQB?*
- *Impose fines on an RSB or RQB and if so, at what level?*

Again we understand this proposal to relate purely to members of the accountancy profession.

[15] Should the Companies Act and the AADB Schemes be amended to allow for the conclusion of cases without public hearings where appropriate and where agreed by the parties?

Please see point 2.10 above.

[16] Do you agree that the FRC should develop a mechanism to enable it to undertake supervisory inquiries into matters of concern, either of individual market events or wider market interest, initially building on its current powers to secure information?

Please see point 2.12 above.

Responses to Questions posed by Jim Sutcliffe in his article in *the Actuary*, dated 24 November 2011

[1]: Do you agree that streamlining the FRC's governance and structure will help ensure that:

[a] FRC regulation of actuaries and actuarial work is proportionate and properly

targeted?

We hope that it will do so. Please see however our comments and concerns at paragraph 2.5 above in relation to the narrowing of the FRC's mission and focus.

[b] The FRC can work effectively with other UK regulatory authorities such as the FSA and the Pensions Regulator?

We hope that it will do so.

[c] The FRC is better able to influence European and international developments?

Insofar as the FRC's role and remit extend to an interest in the international regulation of actuaries, we hope that it will do so.

[d] The FRC is able to maintain its independence from the actuarial profession?

We recognise the importance of the FRC's independent status, although had not identified any threat to that status, in relation to its actuarial role, arising from the current arrangements.

[2]: Do you have any other comments on the proposed reforms?

Please see our comments at sections 1-2 above.

4. Conclusion

As noted at the outset, we are supportive of the FRC's proposals, insofar as they serve to enhance the Profession's relationship with the FRC and, thereby, our collective ability to serve the public interest. We have been encouraged by our mutual progress in the development of that constructive relationship. We would accordingly be concerned, were the currently proposed changes to be seen to

threaten the mutual and positive steps which have been taken in this respect. To a significant extent, this progress is a factor of good communication, including the more intangible aspects of the positive dynamic between all of those involved on behalf of the Profession and the FRC; and not least between staff and Board members at the FRC itself. It is critical in our view that the importance of continuing to enhance the balance and dynamic of this relationship is recognised- and, crucially, that they are not jeopardised- in the context of the currently proposed changes.

More specifically, there are a number of aspects of the current arrangements and relationship which we would consider to be of fundamental importance.

- Drawing on what we say above, it is critical that we continue to be able to work constructively together- albeit recognising of course our respective roles and responsibilities- in our common goal of serving the public interest, including through effective and timely mutual consultation on matters relevant to the profession.
- With the same proviso, we should continue to strive so far as possible to achieve a common understanding and mutually consistent approach in relation to our respective public interest functions.
- It will be key that, in the exercise of its actuarial functions, the FRC continues to be informed, and to be seen to be informed, by adequate appropriate input from professional actuaries; this is critical in our view in ensuring that the FRC continues to carry the confidence and commitment of members of the public and profession alike.
- We have welcomed- and would wish to see continued- the emphasis on principles (as opposed to detailed rules) and outcomes (as opposed to process); both in relation to standard-setting, but also more widely in respect of the FRC's approach to its oversight role. It is important, in our view, that that approach is always informed, and is seen to be informed, by clear regulatory principle and that any temptation towards unjustified 'regulatory creep'- in particular, towards a 'box-ticking' mentality- is properly resisted.

We should welcome the opportunity for further discussion with FRC representatives of the points we have raised in this response and in our answers to the specific questions in the Consultation Document.